



## GOVERNMENT OF PUERTO RICO

Department of the Treasury

**TO:** Mr. Gerardo J. Portela Franco, Executive Director of AAFAF

**FROM:** Francisco Parés Alicea, Assistant Secretary for Internal Revenue Area

**DATE:** July 17, 2018

**SUBJECT:** Involuntary Withholdings on payments for services rendered by Title III Service Providers

**CC:** Mohammad Yassin Mahmud, Chief Legal & Regulatory Officer of AAFAF

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### **I. Statement of Motives**

The Puerto Rico Treasury Department ("Department") has received various inquiries by professional service providers providing services in the title III cases commenced under the Puerto Rico Oversight, Management, and Economic Stability Act (hereinafter referred to as, "Title III Service Providers") regarding the withholding of tax at source by the Government of Puerto Rico on payments made through June 30, 2018, where the amounts billed included services rendered outside of Puerto Rico and expenses to be reimbursed ("Involuntary Withholding").

*FAA* Based on the below analysis, the Department issues this Memorandum to establish the information required to be included in the invoices to be issued by the Title III Service Providers to avoid any Involuntary Withholding and the procedure to be followed by Title III Service Providers to request the refund of any Involuntary Withholding withheld on payments made through June 30, 2018.

Section 1035.01 of the Puerto Rico Internal Revenue Code of 2011, as amended (the "Code"), establishes the categories of income considered from sources within Puerto Rico. As a general rule, services rendered within Puerto Rico are considered Puerto Rico source income subject to tax withholding at source, regardless of the residence or place of incorporation or organization of the service provider. On the other hand, professional services rendered outside Puerto Rico are considered non-Puerto Rico source income, as established in Section 1035.02 of the Code.

Sections 1062.08 and 1062.11 of the Code require that any person that makes payments for services rendered, including the Government of Puerto Rico, has the duty to deduct and withhold a 20% tax at source (in the case of nonresident United States citizens) or 29% tax at source (in the case of nonresident aliens and foreign corporations and partnerships not engaged in trade or business in Puerto Rico) on these payments. In the case of a person engaged in trade or business in Puerto Rico, Section 1062.03 of the Code establishes a 7% withholding of tax at source over the first \$1,500 paid for professional services provided during a calendar year.



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In order for the payor to properly determine the applicable withholding of tax at source, if any, the service providers must segregate in their invoices: (i) the services they performed in Puerto Rico, which constitute Puerto Rico source income subject to a withholding of tax at source, and (ii) the services they performed outside Puerto Rico, which constitute non-Puerto Rico source income. Additionally, the expenses incurred by the service provider related to the services performed, such as lodging and travel expenses, will not be included in the amount subject to withholding, if the same are identified and segregated in the invoice.

Sections 1062.03, 1062.08 and 1062.11 of the Code require that the total payments made for services rendered in Puerto Rico during a calendar year, and the corresponding withholding of tax at source deducted from those payments, if any, be informed in an Informative Return issued to the service provider. Accordingly, the informative returns used to inform those payments are the following:

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- Form 480.6A "*Informative Return - Income not Subject to Withholding*" - annual informative return used to report the total payments for services rendered in Puerto Rico to service providers that are engaged in trade or business in Puerto Rico that are not subject to withholding. These informative returns should be electronically filed at the Department and sent to the service provider not later than February 28<sup>th</sup> of the year following the calendar year in which the payments were made.
  - Form 480.6B "*Informative Return - Income Subject to Withholding*" - annual informative return used to report the total payments for services rendered in Puerto Rico, as well as the corresponding tax withheld at source, to service providers that are engaged in trade or business in Puerto Rico. These informative returns should be electronically filed at the Department and sent to the service provider not later than February 28<sup>th</sup> of the year following the calendar year in which the payments were made.
  - Form 480.6C "*Informative Return – Income Subject to Withholding – Nonresidents*" – annual informative return used to report the total payments made for services rendered in Puerto Rico by a nonresident United States citizens or nonresident aliens or foreign corporations or partnerships not engaged in trade or business in Puerto Rico. These informative returns should be electronically filed at the Department and sent to the service provider not later than April 15<sup>th</sup> of the year following the calendar year in which the payments were made.

In addition, Act 48-2013, as amended, establishes that a 1.5% special contribution will be imposed on the total amount of every professional, consulting, advertising, training or orientation service contract, if in the aggregate exceeds \$50,000, executed by any agency, instrumentality, or entity of the Government of Puerto Rico, public corporation,

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the Legislative Assembly and the Judicial Branch (herein and collectively referred to as, the "Government"). This 1.5% special contribution will be withheld by the Government at the time of issuing the payment for the services rendered.

## **II. Determination**

### **A. Information Required to be Included with Invoices Issued after June 30, 2018 by Title III Service Providers to Avoid any Involuntary Withholdings**

Effective for invoices issued *after June 30, 2018*, all Title III Service Providers must submit with their invoices, a declaration signed under penalty of perjury establishing, among other things, the fees that constitute gross income from sources outside of Puerto Rico and the fees that constitute gross income from sources within Puerto Rico. A sample of the aforementioned declaration is included as an attachment to this Memorandum.

*JAA* In the case of Title III Service Providers that are engaged in trade or business in Puerto Rico and that have an active Total or Partial Waiver Certificate from Withholding at Source for Services Rendered, a copy of said certificate must also be included with every invoice issued.

The above-mentioned documents are required to be able to determine the applicable withholding of tax at source, if any, on the total amount of the payment to be issued. Therefore, if the invoice is not accompanied with the documents indicated above, the Department will assume that the total amount billed is for services rendered in Puerto Rico and will proceed with the corresponding withholding of tax at source.

### **B. Procedure to Request the Refund of Involuntary Withholdings on Payments made through June 30, 2018**

#### **1. Title III Service Providers Required to File an Income Tax Return in Puerto Rico**

Pursuant to Sections 1053.01 and 1053.02 of the Code, the amount of tax withheld at source under Sections 1062.03, 1062.08 and 1062.11 of the Code shall be allowed as a credit against the tax. Therefore, any Involuntary Withholding should be requested by the Title III Service Provider as a credit against the tax determined in their corresponding Puerto Rico income tax return for the year and any amount overpaid could be requested either as a refund or as a credit for other taxable years.

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## 2. Service Providers Not Required to File an Income Tax Return in Puerto Rico

In case of Title III Service Providers that are not required to file an income tax return in Puerto Rico for the year, the Department has established a *temporary process* to request the refund of the Involuntary Withholdings on payments made through June 30, 2018 (the "Request"). The Request must be made by sending the documents indicated below to the Department following the exact same process the Title III Service Provider currently uses to send invoices:

- (i) A declaration signed under penalty of perjury specifying the fees that constitute gross income from sources outside of Puerto Rico and the fees that constitute gross income from sources within Puerto Rico. A sample of the aforementioned declaration is included as an attachment to this Memorandum; and
- (ii) Form SC 2698 "*Claim for Refund of Income Tax Erroneously or Illegally Collected*" ("Form SC 2698"), duly completed and signed. Said form can be obtained through the Department's internet webpage: [www.hacienda.pr.gov](http://www.hacienda.pr.gov), in the *Planillas, Formularios y Anejos* section.

To duly complete Form SC 2698, the Title III Service Provider must complete *all* parts of the form except the "Payment date," the "Tax paid" and the "Tax paid in excess" sections. In addition, the following parts of Form SC 2698 must be completed by the Title III Service Provider according to the information indicated below:

Part of Form SC 2698	Information to be completed
Account number	Title III Service Provider's social security or employer identification number
Taxable year concerning the claim	"2017," "2018" or "2017 & 2018," as applicable
Tax due	Total amount of the Involuntary Withholding that is requested as a refund

Once received, the Department will proceed with the evaluation of the information provided and will respond to the Title III Service Provider considering all the facts and circumstances of the Request.

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The above-mentioned temporary process is *only* applicable for Involuntary Withholdings on payments made through *June 30, 2018*. Effective for invoices issued *after June 30, 2018*, all Title III Service Providers must submit their invoices according to Part II-A of this Memorandum.

For unpaid invoices issued on or before June 30, 2018, the Title III Service Provider must determine whether those invoices were submitted with the corresponding segregation of the services performed within and outside of Puerto Rico and any expense reimbursement being claimed, together with the duly completed declaration, signed under penalty of perjury, indicated in Parts II-A and II-B-2-(i) of this Memorandum. If said invoices do not have the corresponding segregation, or if the declaration has not been submitted, the Title III Service Provider must send the information to the Department following the exact same process currently used to send the invoices.

For any inquiries regarding the items discussed in this Memorandum, please feel free to reach me or Ms. Vivian López, Deputy Assistant Secretary for Internal Revenue Area, via email at [Francisco.Pares@hacienda.pr.gov](mailto:Francisco.Pares@hacienda.pr.gov) and [Vivian.Lopez@hacienda.pr.gov](mailto:Vivian.Lopez@hacienda.pr.gov), respectively.

Cordially,



Francisco Parés Alicea  
Assistant Secretary  
Internal Revenue Area